Mitchell's Musings 5-13-13: The Soft Takeoff

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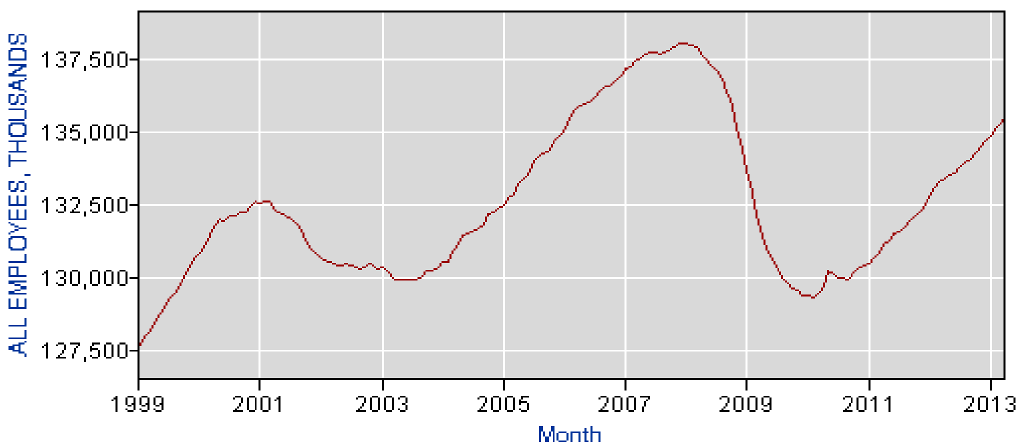
Back in 1969, when the Nixon administration first took office, there was concern among the incoming policy makers about accelerating inflation. It was hoped that a slight touch on the macroeconomic brakes would slow the economy sufficiently to deal with the inflation problem without tipping it into a full blown recession. The phrase "soft landing" came into widespread use to describe such a carefully crafted outcome. In fact, the application of the brakes produced a recession – a hard landing. Soft landings have generally proved to be elusive.

A soft takeoff after a recession seems to be easier to achieve. In fact, since 2009, we have been expanding at a lazy pace. As the chart below shows, we have yet even to bring employment back to its previous peak. And as the headline below from the *LA Daily News* of May 10th shows, the job market – as a consequence - remains soft.

Nonfarm Payroll Employment, Seasonally Adjusted



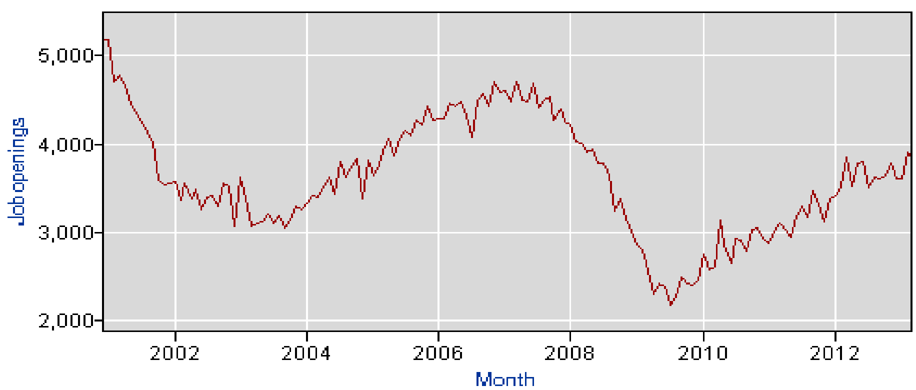
The article under the headline notes that when there are many applicants for available positions, the natural result is some form of job rationing by employers. Such rationing shows up in elaborate hiring processes:

..."It's really frustrating for people," said Cynthia Shapiro, a Woodland Hills-based career strategist and author of the book, 'What Does Somebody Have to Do to Get a Job Around Here?'... Candidates are often forced to endure multiple interviews - sometimes as many as eight - in their quest to land a job, according to Shapiro. "They'll go through a real stringent HR screening, a technical screening, aptitude testing, and then they'll be interviewed by a variety of employees and executives," she said. "They may be asked to do business presentations and even solve problems that can sometimes take weeks to put together."... [http://business-news.thestreet.com/daily-news/story/job-seekers-face-tough-hiring-process-picky-market/1]

It might be noted that while all of this sifting of applicants does succeed in rationing the jobs, it is less clear that all of the hoops that job seekers are put through really accomplish much more than simple rationing. Who knows if the "right" person is ultimately chosen? And maybe the main result of the elaborate process is to create jobs – albeit for those personnel managers in charge of hiring.

One measure of labor-market demand is the number of job openings (vacancies) tallied by the U.S. Bureau of Labor Statistics (BLS). These figures have been collected since the end of 2000, a period which happened to be a business cycle peak. In absolute numbers, job openings did not go back to their previous peak at the top of the next cycle in 2006-2007. And they are well below either peak now. Moreover, demand for labor is actually softer than even these numbers suggest.

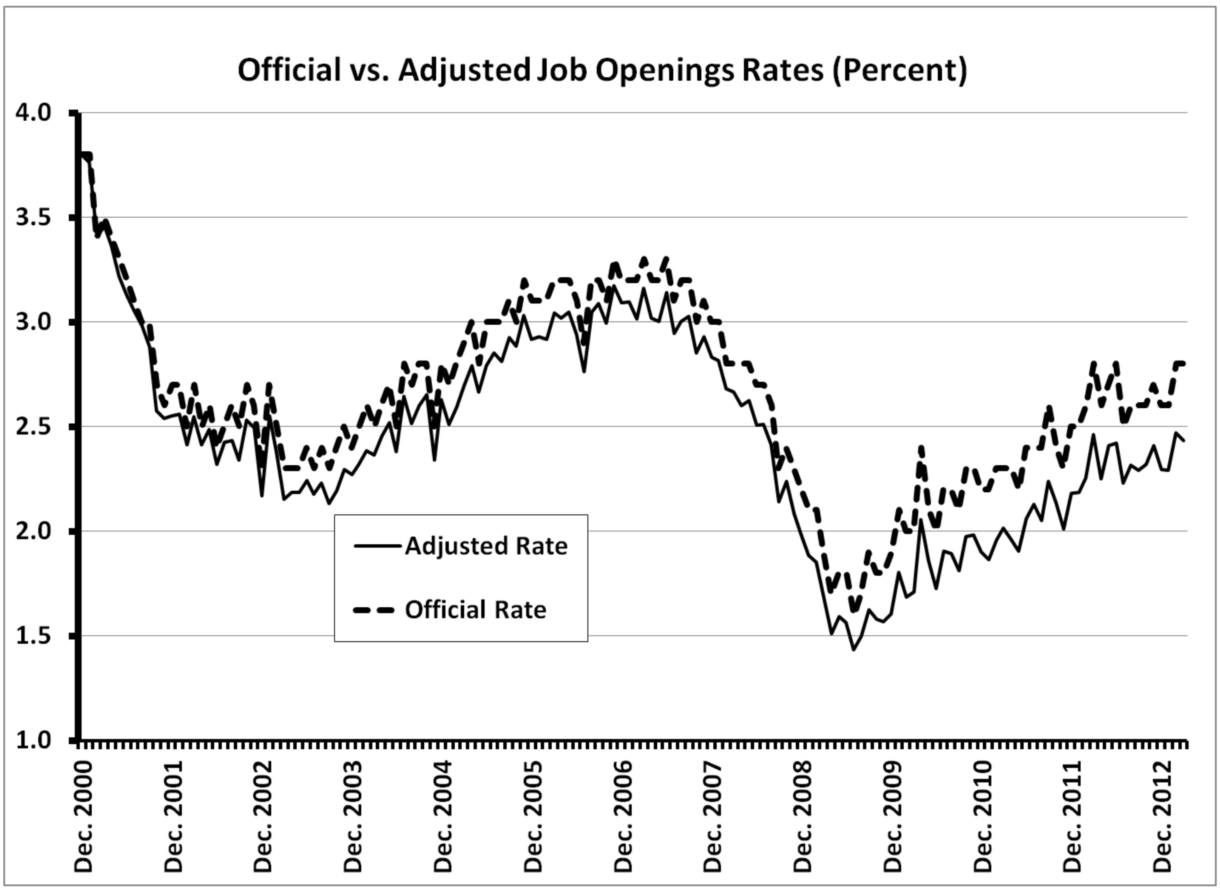
Job Openings, Seasonally Adjusted, 000s



Let's do some back-of-the-envelope calculations. Note that some of total employment consists of *self* employment. There is no usable vacancy concept for such situations; no one declares a vacancy for himself/herself. Measurable vacancies can exist only when there is an employer that is not identical to the employee.

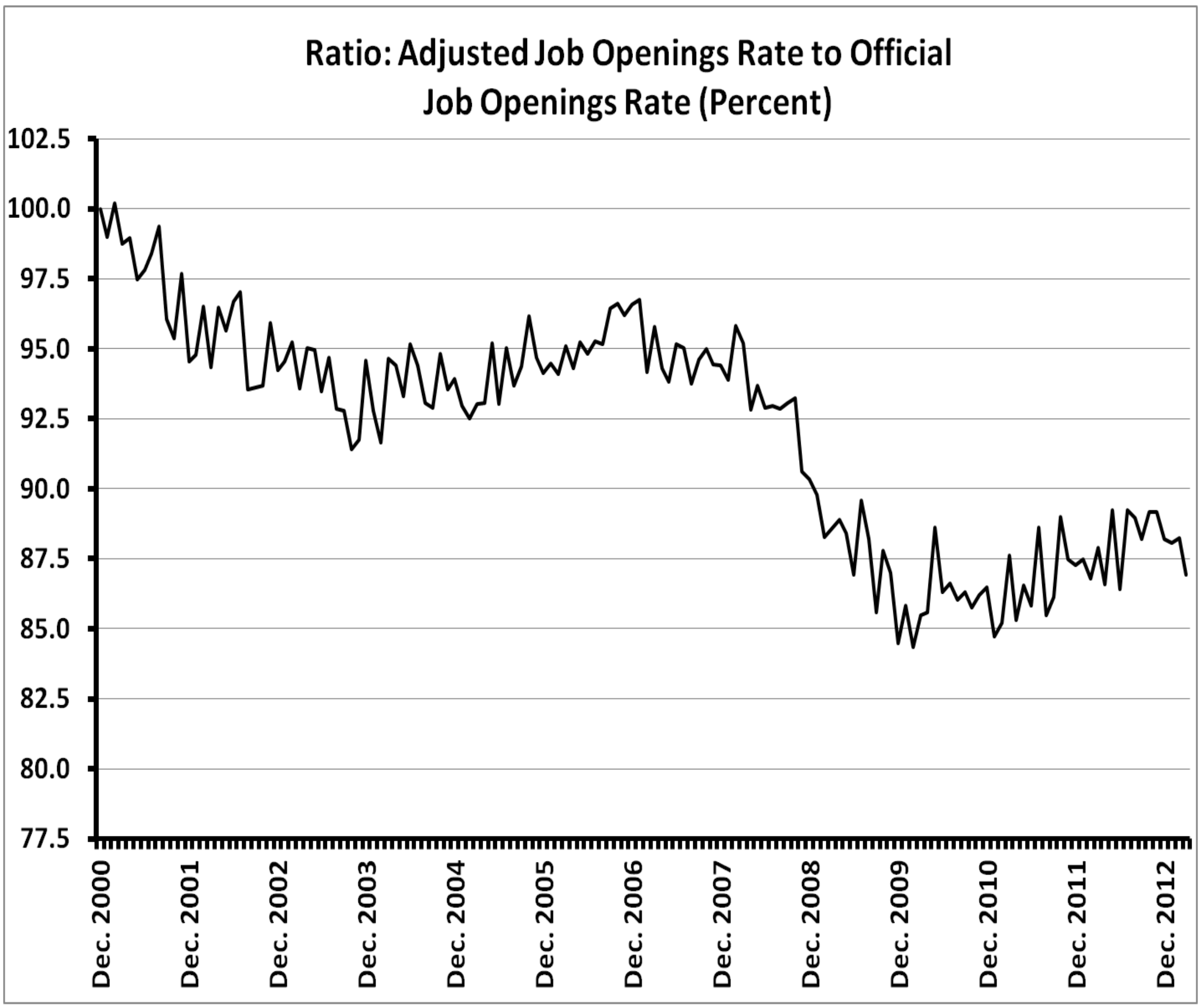
If we take the ratio of nonfarm payroll employment (employment where the employer and employee are not the same) to the civilian population age 16 and over, the resulting figure at the end of 2000 (dot-com boom peak) was 62%. BLS calculates its job openings <u>rate</u> as openings/(employment + openings). At the end of 2000, that rate stood at 3.8%. We can take 62% as an estimate of the full-employment ratio of nonfarm payroll employment to labor-market age population and adjust subsequent payroll employment figures accordingly. Then we can recalculate the post-2000 job openings rates based on what employment "should be" were it not for inadequate demand for labor. That is, we can substitute 62% of the population 16 and over for actual payroll employment in the job openings rate formula.

As the chart below indicates, the adjusted job openings rate falls below the official rate after the end of 2000. Demand for workers at present is officially about three fourths of what it was at the 2000 peak by the official measure. But adjusted for what payroll employment should be, it is somewhat less than two thirds of the job openings rate full employment would produce.



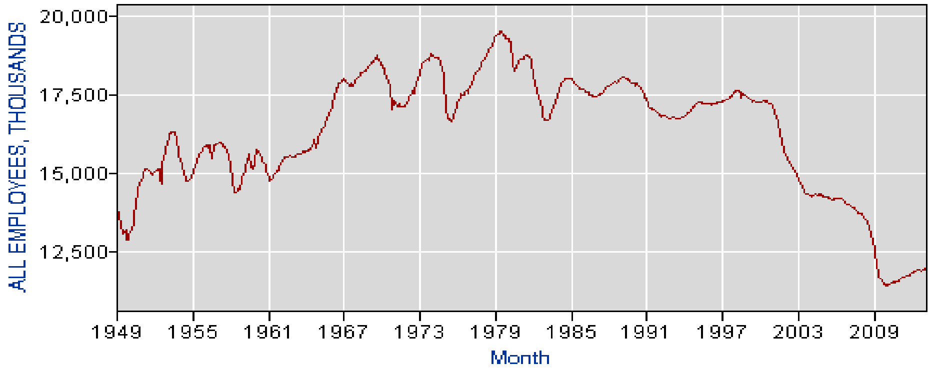
In effect, what we have here is the demand version of the supply-side story that is more often told. Labor-market observers have pointed out that in the current period, many individuals who would otherwise be searching for jobs or might under better circumstances be drawn into employment have dropped out. Such dropping out "improves" the labor market situation as measured by the official unemployment rate since the dropouts are not counted as unemployed. But in fact such dropped out workers are part of a latent labor supply that is not being utilized because of slack demand.

It's unfortunate that we don't have job openings data from BLS in some consistent format before the end of 2000. As a result, we can only hypothesize about the causes of the widening deviation between the official and adjusted job openings rates. It does appear that the labor market at the 2006 peak (housing boom peak) was already softer than at the 2000 peak (dot-com boom peak) and that the gap grew between those peaks. The deviation grew more dramatically after the 2006 peak (the Great Recession and aftermath), as the chart below illustrates. Was anything unusual happening in that period?

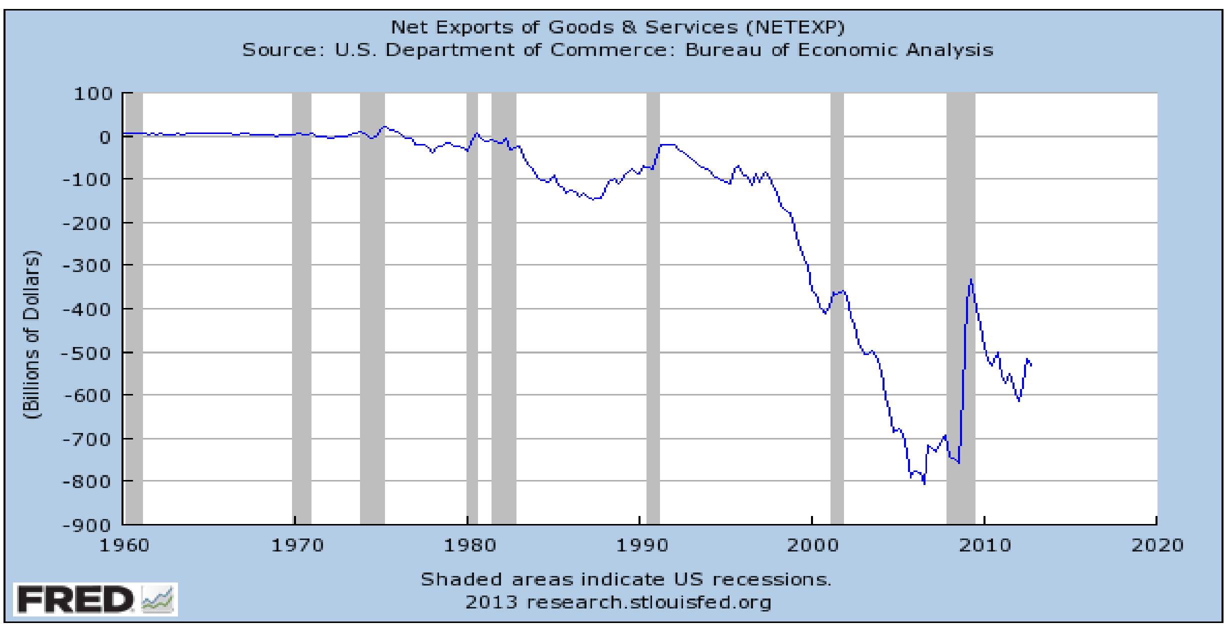


There is at least one notable unusual development and that is what was occurring in manufacturing. As the chart on the next page shows, manufacturing jobs stopped growing in the 1980s and fell off a cliff in the 2000s. Unlike after prior downturns, there was no manufacturing recovery after the recession of the early 2000s. And the manufacturing recovery after the 2008-09 recession is tepid. About 5 million manufacturing jobs have disappeared since 2000.

Manufacturing Payroll Employment, Seasonally Adjusted



Of course, there is nowadays fashionable talk about manufacturing jobs "coming back." Presumably, the coming back refers to returning from outsourcing abroad, mainly to China. But as the chart above makes clear, whatever coming back of manufacturing is going on is not on a track to return even to the level of2000. It is also unlikely that jobs in other (non-manufacturing) sectors that went abroad are going to be coming back anytime soon. And the softness of the labor market isn't confinable to particular sectors that were outsourced.



Lost jobs in any one sector push workers - who would otherwise have been employed there - to seek jobs in other industries or to become part of the latent labor supply noted earlier. As we have noted in past musings, the softness in the labor market is reflective – not of global competition *per se* – but of the U.S. net export imbalance (deficit) shown above. That imbalance, in turn, has much to do with exchange rate policies undertaken abroad *and* with the lack of response to those policies domestically. Apart from some Congressional grumbling, no real steps have been taken to address what is ultimately a drag on the labor market and on the recovery of the labor market. The numbers are there; the political will to respond to those numbers isn't there.

The flip side of the net export imbalance is a rising national net debt to foreigners which ultimately is unsustainable. If you keep spending more abroad on imports than you earn in exports, net debt piles up. It seems evident that eventually, there will be some "correction." Until then, we may be condemned to soft takeoffs. However, when the correction occurs, the landing may well be hard. You didn't read it here first; many others have said the same. But nonetheless, you *did* read it here.